IN THE

# Supreme Court of the United States

**OCTOBER TERM, 1942.**

**No. 246.**

CHARLES CORYELL, *et al.*,
*Petitioners,*

—against—

JOHN S. PHIPPS and GEORGE J. PILKINGTON,
*Respondents.*

## BRIEF FOR PETITIONERS.

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Argument:

I—The holdings of the courts below that respondent Phipps as a shareholder in the Seminole Boat Company is not liable to petitioners because it was not shown that there was "fraud or other improper conduct or purpose in the creation or continued existence of the corporation" or that "the corporation was an artifice and a sham designed to execute illegitimate purposes" are erroneous. The rule in this Court, in other circuits, and in the State of Florida, is that when a corporation is not supplied with funds necessary for corporate independence; when officers of the corporation are subject to control and domination by the stockholders and have no true independence of action, receive no compensation for their services, and have no interest in the corporation, and are dependent upon approval of stockholders in cases where substantial repairs are needed; when the corporation is without credit of its own and must rely entirely upon

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## BRIEF FOR PETITIONERS.

### Opinions Below.

The findings of fact, and conclusions of law of the District Court are officially reported in 39 F. Supp. 142, and are printed in the record (R. 3582). The opinion of the Circuit Court of Appeals, filed June 9, 1942, is officially reported in 128 F. (2d) 702, and is printed in this record (R. 3645).

### Jurisdiction of this Court.

The suit is in admiralty. The losses and damages were sustained by water borne craft afloat upon navigable waters. The jurisdiction of this Court is invoked under Section 240 of the Judicial Code, as amended by the Act of February 13, 1925; 43 Stat. 938, 28 U. S. C. A. Section 347.

### Statement of the Case.

Petitioners, Charles Coryell and forty-four other boat owners, instituted a suit in Admiralty in the United

States District Court for the Southern District of Florida against the respondents Phipps and George J. Pilkington* to recover damages for the destruction of some forty-five vessels owned by petitioners, as a result of a fire which occurred on June 24, 1935, while the vessels were afloat at Pilkington's covered storage basin, Fort Lauderdale, Florida. The fire was caused by an explosion of gasoline fumes in the engineroom of the yacht "Seminole", then registered in the name of Seminole Boat Company. Respondent Phipps alleged that there was no negligence, but that even if there had been negligence, such negligence was that of the Seminole Boat Company and was not his negligence, and that, even if he were negligent, he was entitled to the benefits of the Limitation of Liability Statute. For the text of this Statute, see Appendix A.

Both Courts below concurrently found that the gasoline fumes had escaped into the engineroom of the "Seminole" because of the leaky condition of the "Seminole's" gasoline tanks and installation, which became defective with the "passage of time" (R. 3587-8, 39 F. Supp. 142 at p. 144; R. 3648, 128 F. (2d) 702, at 704). Both Courts then held that the Seminole Boat Company was liable for the damage sustained by your petitioners because of the negligence thus found, but that Phipps was not liable (R. 3588, 39 F. Supp. 145; R. 3648, 128 F. (2d) 704) because the negligence was that of the Seminole Boat Company, and not that of Phipps, who was a mere stockholder in that company. Thus the issue of negligence is definitely determined by the findings of both Courts below that the damage to petitioners' vessels was due to a defective condition of the yacht "Seminole". Those findings are in the following language:

* The claim against Pilkington, operator of the storage basin, was not pressed in the Circuit Court of Appeals and is not pressed here.

The District Court:

> "The presence of gasoline fumes in the engine room, I find was the proximate cause of the damage done to the vessels of libellants."
>
> * * * *
>
> "The Seminole Boat Company was responsible for the proximate cause. It was not negligence to have converted a steam yacht into a gasoline propelled vessel, and from the evidence it is clear there was no negligence in the original installation of the tanks which were used on the 'Seminole' for gasoline storage. *But with the passage of time some part of the machinery or equipment did leak* and the great possibility of damage attendant upon the use of gasoline, brings into play the principle that negligence may be based upon circumstantial evidence alone. The respondent argues that there must have been some third person agency intervening which brought about the means whereby gasoline escaped with attendant fumes. There is no evidence of this, and we get into the realm of conjecture. *Just when the defective condition of the tanks made them leaky is in doubt.* Expert testimony on this is an unsatisfactory character of evidence. *I am satisfied, and find, that there were gasoline fumes present in the engine room, and that their ignition into combustion and fire caused the damage. For this the Seminole Boat Company was liable.* Whether the Seminole Boat Company could limit liability is not necessary to decide. That is not in the case" (R. 3587-88, 39 F. Supp. at p. 144).*

The Circuit Court of Appeals concurred in these findings, saying:

> "The basic dispute turns upon the ultimate facts, for when they have been ascertained the principles of law applicable thereto are well settled. This being an appeal in admiralty, the findings of fact made by

* Italics in quotations ours throughout this brief.

the court below are not binding upon us, but we think the evidence preponderates in favor of the findings made in each material instance. Under the evidence, the case presents itself in this aspect: Appellants' vessels sustained damages by reason of the negligence of the Seminole Boat Company" (R. 3648, 128 F. (2d) 704).

Later in the opinion while discussing the issue of limitation of liability, the Court refers to "the defective condition obtaining upon the 'Seminole'" (R. 3649, 128 F. (2d) 704).

The defense based upon the issue of negligence is no longer open to respondent Phipps in this Court, *Just* v. *Chambers*, 312 U. S. 383, 385. So also since respondent Phipps has not presented any questions for determination to this Court, he may not question the correctness of any determination not raised by the petitioners. *The Mahrdal Baxter, Jr.*, 277 U. S. 323. The issues before this court are: was the corporate setup of the Seminole Boat Company such that Phipps should have been held liable for the negligence found and, if so, was Phipps entitled to limit his liability to the value of the damaged yacht "Seminole"?

Because the Seminole Boat Company was an empty shell and the yacht "Seminole" was a complete wreck, the decision of the lower courts meant that the petitioners were without redress. Although at the time of the loss Mr. John S. Phipps and his sister, Mrs. Guest, were both shareholders of the Seminole Boat Company, suit was brought against Mr. John S. Phipps alone.*

* In admiralty each tort feasor is liable for full damages *The Atlas*, 93 U. S. 302, and the *Virginia Ehrman*, 97 U. S. 309, 317. When by negligence the vessel sets fire "to one adjoining" or causes a collision, all the part owners are answerable *in solido* (*Parsons on Shipping & Admiralty*, Vol. I, 106. *Parsons on Maritime Law*, 94). See also: 58 Corpus Juris, Title Shipping, p. 303, Par. 424; *Scull* v. *Raymond*, 18

[Footnote continued on following page]

## Facts.

The yacht "Seminole", prior to February 16, 1929, was registered at the Custom House at Miami as being solely owned by the respondent John S. Phipps (Exhs. 30 and 31, Certificates of License offered, R. 249).

The District Court found, that during February 1915, respondent Phipps purchased a half interest in the yacht "Seminole", then a steam yacht, from his brother, H. C. Phipps. During 1922, her steam plant was removed and gasoline engines and their necessary appurtenances were installed (Fdg. 2, R. 3582). At that time, four cylindrical tanks, to be used for carrying gasoline to drive the yacht's engines, were placed in a compartment which had formerly been used as a coal bunker (R. 376, 572-3). The tanks completely filled the coal bunker, and it was impossible to inspect them properly without removing the bulkheads of the compartment (R. 135-6, 142-3, 171-2, 383, 397, 573-4, 840-42, 974-5, 2231, 2248-9). In late 1928 or early 1929, the two brothers each sold their one-half interest in the "Seminole" to Seminole Boat Company, a Delaware corporation, which had been formed by them for the purpose of taking title to the "Seminole" and operating her under charter for hire. Each of them received one-half of the stock of the company. The "Seminole" was, in fact, chartered on several occasions in 1929 and 1930 but no charterer was found for her after 1930 or for more than five years preceding the fire (Fdg. 3, R. 3583).

The officers and directors of the corporation were Paul

[Footnote continued from preceding page.]

Fed. 547. It follows that a determination of these issues in favor of petitioners will permit a full recovery by them of their damages from the respondent Phipps, leaving him to seek such contribution from his sister as he may be advised. The interest of Mrs. Guest in the "Seminole" and in the corporation did not appear, and were unknown to libellants when suit was brought, or until established by respondent's testimony at the trial.

Scott, President, R. C. Alley, Vice-President and Roy H. Hawkins, Secretary-Treasurer. These men, as officers of the corporation, assisted by James F. Riley, advised by certain boat captains, operated, controlled, maintained and managed the vessel from the time of her purchase by the corporation down to and including the time of the fire (Fdg. 4, R. 3583).

In March 1935, when an opportunity to sell the vessel arose, H. C. Phipps wished to sell but respondent Phipps did not. Mrs. Amy Guest, a sister of H. C. and John S. Phipps, thereupon purchased the interest of H. C. Phipps. No other change in the operation, control, maintenance or management of the vessel occurred prior to the fire (Fdg. 5, R. 3584).

Scott, Alley and Hawkins were selected by respondent Phipps and his brother to be officers and directors of the corporation Seminole Boat Company. They, as well as Riley, were so-called "family representatives" of the Phippses (R. 1911, 1944, 1956) and were employees of certain other corporations in which the Phipps family were the shareholders and principals (R. 1355, 1470, 1478-81, 1593, 1590-1). As such, they were subject to the orders of the respondent Phipps and his brother, and subject to their call, as well as that of other members of the Phipps family, to attend to their personal business matters (R. 1451-2, 1477, 1485-6, 1582). They were not stockholders and had no interest in the Seminole Boat Company (R. 1363), nor did they receive any compensation from Seminole Boat Company (R. 1582-3). Their salaries were paid by the general paymaster of the Phipps' interests (R. 1353-4, 1486) and no part of such salaries were charged to Seminole Boat Company (R. 1354-5, 1486, 1582-3). Their services to Seminole Boat Company were gratuitous and undertaken for the accommodation of the Phippses (R. 1395).

The corporation was not furnished with capital funds

necessary for an independent corporate existence. The only cash paid into its treasury upon organization was $100, a nominal payment of $50 from each of the stockholders. Its bank account was closed after June 2, 1931 because it was so inactive (R. 1472, 1477). The bills of the corporation for expenses of the vessel were paid by other Phipps corporations* and charged on their books to Seminole Boat Company (R. 1281, 1324-5) until repaid periodically by respondent Phipps and his brother (later his sister) directly to the corporations which had advanced the money. The corporate books contained only a record of such repayments by the Phipps made long after the debts were incurred. Exhibit D (offered, R. 1659, see reprint accompanying record) is respondent's own summary of the method by which the corporation was financed.

These family representatives of the Phipps performed the same functions for the "Seminole" after incorporation as they had done before that event, and they acted for the "Seminole" in the same manner as they acted for other vessels owned directly by respondent Phipps and members of his family without the benefit of the corporate form (R. 1361, 1368-70, 1398-9, 1454, 1584-6, 1532, 1596-7). They consulted with the stockholders and acted subject to their directions on all except minor routine matters (R. 1282-3, 1381-2, 1297-9, 1300-1, 1333, 1886-7).

Due to the fact that the corporation had no funds of its own and was dependent on the payment of its debts and expenses by the Phippses (R. 1400, 1941), the officers of the corporation could not incur expenses for more than nominal sums without express authority from the Phippses. Hawkins said the limit was $500 (R. 1380-1); Riley, $300 (R. 1505); see for instance authorization of $300 for repair of generator (R. 1505-6, 1596, Exh. 3-T1, R., Vol. VI, p. 18, offered, R. 1507).

* Boulevard Mortgage Company and Palm Beach Company.

As long as the "Seminole" remained in existence the respondent Phipps continued to make personal use of her whenever he desired to do so (R. 340, 1387, 1898-9, 1915, 438, 507, 1507-8, 1643-7, 1917) by merely informing the officers of the corporation of his wishes (R. 1914-5). They recognized his authority (R. 1387-8). The only limitation on his right to use the vessel which he recognized was his personal preference to charter, if a charter was available so that he could have the charter hire (R. 1915; see also R. 1886). For several years after the incorporation, the yacht "Seminole" continued to be registered with the New York Yacht Club as the personal yacht of respondent Phipps (R. 1965, 1965-7; Answer (i) R. 89).

## Conclusions of the District Court With Respect to Liability of the Respondent Phipps.

The District Court held that in spite of the circumstances of the organization and control of Seminole Boat Company by the respondent Phipps and his brother, shown by the respondent's own evidence, Seminole Boat Company acted "as a legal non-conductor between Phipps on the one hand and the libellants and Pilkington on the other, *because there was no fraud or other improper conduct or purpose* in the creation or continued existence of the corporation" (R. 3589). The Court said:

> "The organization of the corporation, Seminole Boat Company, was a natural normal development of ownership of a pleasure yacht, *free from any fraud or ulterior motive in the inception of its chartering and creation.* Likewise, it was free of any of the other elements, treated in the reported and cited cases *incident to the presence of bad faith*, which apply the doctrine of piercing the corporate veil" (R. 3587).

The Court said further:

> "Furthermore, the character of the negligence which this record discloses is the failure to do or perform a duty, or nonfeasance. Such failure of duty does not give rise to an application of the *alter ego* or agency doctrine" (R. 3587).

In both of these respects we submit the District Court was in error and our argument under Point I is in support of this position.

## Conclusions of the Circuit Court of Appeals With Respect to Liability of the Respondent Phipps.

Upon appeal to the Circuit Court of Appeals that Court held that, since petitioners' vessels sustained damage by reason of the negligence of Seminole Boat Company, "in order to hold Phipps to personal liability, appellants [petitioners] had the burden of establishing by a preponderance of the evidence, that the corporation was *an artifice and a sham designed to execute illegitimate purposes* in abuse of the corporate fiction and the immunity that it carries, and that its activities in reality were those of Phipps personally" (R. 3648).

We submit that the Court was in error in this statement and we support our position by the argument under Point I.

## Limitation of Liability.

Respondent Phipps also set up the defense of limitation of liability under Sections 4283 and 4284 of the Revised Statutes of the United States* and the statutes supplementary thereto and amendatory thereof (R. 63).

* U. S. C., Title 46, Secs. 183, 184, 185, 186. Printed as Appendix A to this brief.

## Petitioner's Contention on the Issue of Limitation.

Petitioners contend that since the concurrent finding below was that, with the passage of time, some part of the machinery of the yacht did leak, with the result that gasoline fumes entered the engineroom and caused the fire, these facts in themselves establish circumstances which deprived respondent Phipps of the benefit of the limitation statute; and that such a condition necessarily indicates a failure to inspect, or to provide an adequate system of inspection. Otherwise this defective condition would have been discovered during "the passage of time".

Your petitioners further contend that the officers and directors of the corporation selected by respondent Phipps to manage and operate his vessel, and Riley, to whom they later entrusted complete control and management of the vessel for a long period before the fire, were the *alter ego* of respondent Phipps; that their negligence, knowledge and privity were the negligence, knowledge and privity of the respondent Phipps; that their failure to provide an adequate system of inspection by competent persons, and proper maintenance, constituted negligence, knowledge and privity on their part which was in legal effect the negligence, knowledge and privity of the respondent Phipps, precluding limitation of liability; and that respondent Phipps could in no event establish his claim for limitation of liability without showing that the persons appointed by him to manage the vessel were competent.

Respondent's evidence failed to show any qualification or previous experience of the officers and directors of the corporation, Scott, Alley and Hawkins, for management of the yacht "Seminole" or any vessel property. Beginning in April 1931, by direction of Scott, President of the corporation, the "Seminole" was placed in storage at Fort Lauderdale and subsequent thereto, she was continuously in storage up to the time of the fire except for only four

brief occasions. By direction of Scott, the vessel, while in storage, was placed in the "control and management" of Riley, who was instructed "to inspect her regularly" (R. 1454-7, 1472, 1480). Riley conceded his inexperience and incompetence to inspect the vessel (R. 1595-6; see also R. 1637, 1640-1).

The District Court held that even if the liability were held to be that of the respondent Phipps "*the character of negligence shown by this record* was such that Phipps, as an individual, would not be precluded from asserting as a limitation of liability under the statute" (R. 3588). The Court had previously held that "The character of the negligence which this record discloses is the failure to do or perform a duty, or nonfeasance" (R. 3587).

We shall show under Point II of this brief that this holding is not supported by authority and is wrong in principle.

The Circuit Court of Appeals on the question of limitation of liability held independently of the District Court that "the evidence affirmatively establishes that no actual privity to or knowledge of the defective condition obtaining upon the 'Seminole' was attributable to Phipps personally and that none could be imputed to him *since he had exercised due care and diligence in selecting competent men to man the vessel, and had imposed upon them full duties as to inspection and maintenance of her*" (R. 3649).

Petitioner contends that the "imposition upon" the men selected by respondent Phipps of "full duties as to inspection and maintenance" of the "Seminole" made them the *alter ego* of the respondent Phipps and that consequently their negligence, knowledge and privity were the negligence, knowledge and privity of the respondent Phipps. Since the respondent Phipps had delegated to them the entire responsibility for inspection and maintenance of the vessel, their negligence, knowledge and privity were the negligence, knowledge and privity of

respondent Phipps. We shall support this proposition under Point III of this brief.

The statement by the Circuit Court of Appeals that the men selected by the respondent Phipps upon whom he imposed full duties as to inspection and maintenance were competent, was not a concurrent finding. The District Court made no finding with respect to the competency of any of these men. The District Court found only that the "nature of the negligence" (R. 3588), *i. e.*, non-feasance as opposed to mis-feasance (R. 3587), was not such as to preclude the respondent Phipps from limitation of liability. The Circuit Court of Appeals in its cursory examination of the record failed to note that there is no evidence whatever in the record of the competency or experience of the officers and directors, *i. e.*, Scott, Alley and Hawkins, and that Riley, who was entrusted by them with control and management of the vessel and the duties of regular inspection, was concededly inexperienced and incompetent. We shall support this proposition under Point IV of this brief.

## Questions Presented to This Court by the Petition for a Writ of Certiorari.

1. Whether the individual owner of a yacht can escape his responsibilities and liabilities as such owner and secure insulation from liability by forming a corporation to own his vessel

(a) When the corporation is not supplied with capital funds necessary for corporate independence;

(b) When the corporation is officered by individuals of his own choosing who

1. are personally holden to him and obligated by virtue of their situations to do his bidding and to attend to his personal business;

2. receive no compensation from the corporation for their services;

3. have no interest in the corporation;

4. are limited in their discretion and in the management of the vessel by the fact that the corporation has no funds of its own and is dependent on the stockholders for the payment of its debts, and the officers must therefore consult with the stockholders before expenditure of any more than nominal sums.

(c) When the corporation is without credit of its own, and is dependent for its existence upon the credit of the stockholders who mually pay its debts, which are paid in the first instance by other corporations controlled by the stockholders, such debts aggregating over a period of a few years several times the value of the vessel, the sole corporate property.

(d) When such owner retains control and use of the yacht and continues to use the yacht as desired for his personal pleasure, the corporate officers without corporate action recognizing his right, and such owner acknowledges no limitation of that right except his personal preference for charter hire when a charter is available.

2. (a) Whether an owner of a vessel can escape the imputation of knowledge and privity inherent in a dangerous condition of the vessel caused by progressive deterioration of machinery and equipment which leaked, and tanks which became "defective" and "leaky" with the passage of time, by the appointment of agents, competent or otherwise, to whom he transfers "full duties" of "inspection and maintenance"?

(b) Whether an agent, to whom an individual owner of a vessel transfers all his duties and responsibilities for

inspection and maintenance of his vessel, is not the *alter ego* of such owner? and whether the negligence, knowledge and privity of such an agent, or agents, is not the negligence, knowledge and privity of such owner as was held by the Circuit Court of Appeals in the Second, Sixth and Ninth Circuits?

3. Whether the failure of an owner to provide for competent management and proper inspections and for an adequate system of inspection of his vessel by competent persons does not require the denial of limitation of liability on the ground of privity and knowledge as held in the Second, Sixth and Ninth Circuits?

The petition for a writ of certiorari was granted by this Court on October 12, 1942.

## Argument.

### I.

**The holdings of the courts below that respondent Phipps as a shareholder in the Seminole Boat Company is not liable to petitioners because it was not shown that there was "fraud or other improper conduct or purpose in the creation or continued existence of the corporation" or that "the corporation was an artifice and a sham designed to execute illegitimate purposes" are erroneous. The rule in this Court, in other circuits, and in the State of Florida, is that when a corporation is not supplied with funds necessary for corporate independence; when officers of the corporation are subject to control and domination by the stockholders and have no true independence of action, receive no compensation for their services, and have no interest in the corporation, and are dependent upon approval of stockholders in cases where substantial repairs are needed; when the corporation is without credit of its own and must rely entirely upon the credit of its stockholders; and when the stockholders retain the use of, and do use, the corporate property as their own, the stockholders who so act are in fact principals and liable for the negligent acts of the corporation and its agents.**

The District Court in holding that the respondent Phipps was not liable for the negligence found, based its conclusion upon the proposition of law that the organization of the Seminole Boat Company "was free from fraud or ulterior motive in the inception of its chartering and creation" (R. 3587). The Court held further that the Seminole Boat Company was a legal non-conductor between Phipps on the one hand and libellants (petitioners) and Pilkington on the other, "because there was no fraud or improper conduct or purpose in the creation or continued existence

of the corporation" (Concl. 2, R. 3589; 39 F. Supp. 142, at p. 145). The Circuit Court of Appeals held that "in order to hold Phipps to personal liability, appellants had the burden of establishing by a preponderance of the evidence, that the corporation was an artifice and a sham designed to execute illegitimate purposes in abuse of the corporate fiction and the immunity that it carries, and that its activities in reality were those of Phipps personally" (R. 3648).

We submit that both of these holdings are in conflict with the decision in *Chicago, Mil. & St. Paul R. R. Co.* v. *Minn. Civic Assn.*, 247 U. S. 490, at page 501, which laid down the following rule:

> "where stock ownership has been resorted to, not for the purpose of participating in the affairs of the corporation in the normal and usual manner, but for the purpose, as in this case, of controlling a subsidiary company so that it may be used as a mere agency or instrumentality of the owning company or companies" * * * "the courts will not permit themselves to be blinded or deceived by mere forms of law, but regardless of fictions, will deal with the substance of the transaction involved as if the corporate agency did not exist and as the justice of the case may require."*

That the substance of the transaction involved is the determining factor in determining whether corporate agency did exist has been repeatedly held by this Court;

*U. S.* v. *Lehigh Valley R. R. Co.*, 220 U. S. 257;

* This statement as repeated in *U. S.* v. *Reading Co.*, 253 U. S. 26, 62, 63, although made with respect to a case involving the commodities clause, has as pointed out by Frank, *C. J.*, "become a classic statement applied generally in cases piercing the corporate veil." *Weisser* v. *Maysam Shoe Corp.*, 127 F. (2d) 344, 346, note 4. See also an article entitled "Insulation from Liability Through Subsidiary Corporations" by William O. Douglas and Carrol M. Shanks, 39 Yale Law Journal, p. 193, where the cases decided before 1929 are collected.

*McCaskill Co.* v. *U. S.*, 216 U. S. 504;
*Linn Timber Co.* v. *U. S.*, 236 U. S. 574;
*Southern Pacific Co.* v. *Lowe*, 247 U. S. 330;
*U. S.* v. *Reading Co.*, 253 U. S. 26;
*Gulf Oil Corp.* v. *Ellenbogen*, 248 U. S. 71;
*Chicago, Milwaukee & St. Paul R. R. Co.* v. *Minn. Civic Assn.*, 247 U. S. 490;
*Davis* v. *Alexander*, 269 U. S. 114;
*Gregory* v. *Helvering*, 293 U. S. 465;
*Consolidated Rock Co.* v. *DuBois*, 312 U. S. 510, 524.

In none of these cases is "fraud" or "other improper conduct or purpose" or "illegitimate purpose" made a test of liability of the parent (individual or corporate) of a corporation. On the contrary, the Courts have held that *domination and control* of the subsidiary by the parent creates liability.

The Circuit Courts of Appeal in other circuits than the Fifth have taken a like view.

In *The Willem van Driel, Sr.* (C. C. A. 4), 252 F. 35, certiorari denied 248 U. S. 566, an Admiralty case, the Circuit Court of Appeals for the Fourth Circuit held that, where the Pennsylvania Railroad Company through stock control dominated a company called the Central Elevator Company, the Pennsylvania Railroad Company was liable for the negligence of the Central Elevator Company in the operation of a grain elevator which caught fire and damaged the S. S. "Willem van Driel, Sr." The Court held that the liability of the Pennsylvania Railroad Company depended upon whether the Elevator Company was in substance a mere corporate agent or instrumentality of the Pennsylvania Railroad Company. It found that there was such a complete dominance and control of the Elevator Company by the Pennsylvania Railroad Company that the Elevator Company was a

"mere puppet" of the Railroad Company. The Court then adopted the language of Judge Wallace in *Lehigh Valley R. R. Co.* v. *DuPont* (C. C. A. 2), 128 F. 840, as follows:

> "Applying the language of Judge Wallace in *Lehigh Valley Railroad Co.* v. *DuPont*, 128 Fed. 840, 64 C. C. A. 478, the potential and ultimate control of all its property and business affairs of the elevator company was lodged in the railroad company, and this control was exercised as completely and as directly as the machinery of corporate organisms would permit. Such complete dominance and control by the railroad company made the elevator company its mere puppet. *United States* v. *Del. Lack. & West. R. R.*, 238 U. S. 516, 35 Sup. Ct. 873, 59 L. Ed. 1438" (252 Fed. 35, 39).

The *Willem van Driel, Sr.*, was followed by the Circuit Court of Appeals for the Fourth Circuit in *Luckenbach S. S. Co. et al.* v. *W. R. Grace & Co., Inc.* (C. C. A. 4), 267 F. 676, 681, and in *The Centaurus* (C. C. A. 4), 291 F. 751.

The same result was reached in the Second Circuit.

> *Lehigh Valley R. R. Co.* v. *DuPont* (C. C. A. 2), 128 F. 840.

The Circuit Court of Appeals for the Second Circuit followed the last cited case in *Lehigh Valley R. R. Co.* v. *Delaware* (C. C. A. 2), 145 F. 617, and in *Costan* v. *Manila Electric Co.* (C. C. A. 2), 24 F. (2d) 383, 384, and in the very recent case of *Weisser* v. *Marsam Shoe Corporation, et al.* (C. C. A. 2), 127 F. (2d) 344.

*The Willem van Driel, Sr.*, *Luckenbach S. S. Co.* v. *W. R. Grace & Co., Inc.* and *Costan* v. *Manila Electric Co.* were all cited by this Court in the case of *Consolidated Rock Co.* v. *DuBois*, 312 U. S. 510, 524.

In the case of *The Silver Palm* (C. C. A. 9), 94 F. (2d) 776, 780, the Circuit Court of Appeals for the Ninth Circuit held that the operating company of the vessel named was the *alter ego* of the owner. It stated that under the circumstances of that case the group of companies involved "constituted a family affair".

The Circuit Court of Appeals for the Sixth Circuit, in the case of *In re Lake's Transit Corporation and James Playfair*, 81 F. (2d) 441, held that Playfair was personally liable as owner of the vessel involved, since the facts showed that he was the real party in interest, although it was claimed that title was held by a corporation in which Playfair and his family owned 90% of the stock. In none of these cases did the Court base its decision upon fraud, nor upon sham or illegal purpose. These decisions all rest upon the ground that the company had no independent existence and was in fact merely the *alter ego* of the stockholder.

The Florida cases are very clear on this point.

*Biscayne Realty & Ins. Co. v. Ostend Realty Co.*, 109 Florida 1, 8*; 148 So. 560, is the leading Florida case. In summing up its reasons for reversing a decree of the trial Court where it had declined to pierce the corporate veil, the Court said:

> "In the view we have of the case *it is unnecessary to say that the Ostend Realty Company was organized for an illegal purpose*, nor to say that the ownership of all its stock by Clarence M. Busch dissolved it. That is not necessary to a determination of the case. It is sufficient to say that the original bill, the answers thereto, and the evidence disclose a state of facts, at least suggest such facts, as would require

* Note that the opinion reported at page 1 is superseded by that beginning at page 8.

a court of equity* to look beyond the mere form of the corporate entity to the person who was the sole beneficiary of its activities, directed and managed the transactions, used the corporate name at his pleasure, incurred financial obligations in its name, conveyed to himself the corporate lands when he so desired, received all money paid to the corporation by way of consideration in its transactions, if any, assumed obligations primarily assumed in the corporate name which were originally intended to be taken over by him, used the name of the corporation and set it up as his principal, assumed the act as its agent when in fact the act in the corporate name was his act, and his act that of the Corporation. In the circumstances the interests of the two cannot be distinguished. In these transactions the Corporation by name became indebted to third persons. It was the *alter ego* of the defendant Busch" (109 Florida 22).

This case was followed by *The Third Avenue Company, et al,* v. *May Rodine Kirby*, 111 Florida 46, 149 So. 30, opinion filed May 30, 1933, petition for rehearing denied October 17, 1933. That case also involved a creditors' bill, whereby creditors of the defunct "The Third Avenue Company," sought to charge Henry C. Phipps, John S. Phipps (the respondent herein), Biscayne Boulevard Company (a Phipps' corporation), and Palm Beach Company (the second of the Phipps' Companies used to finance the Yacht "Semitole"), Phipps Realty Company and Mortgage Discount Company, with the debts of The Third Avenue Company. In that case the allegations of the original bill were summarized by the court as follows:

"Through many allegations, made lengthy by de-

* Although a Court of Admiralty is not a Court of Equity it administers justice on equitable principles—*Watts* v. *Camors*, 115 U. S. 353, 361; *United States* v. *Cornell Steamboat Co.*, 202 U. S. 184, at p. 194.

tailed accounts of numerous alleged transactions, the fact is set up in reasonably clear and certain language that the Phippses organized and owned the five corporations; that while their names do not appear as stockholders or officers in any one of the corporations, they were nevertheless the owners of them, dominated, controlled and directed them through others, the employees of the Phippses, who used the names of such employees as officers and owners of the capital stock, although they paid nothing for their stock and constituted as such officers merely mouthpieces or agents for the Phippses who furnished the money for the stock held by their employees and who manipulated, managed and controlled all the activities of the different corporations solely and exclusively for the benefit of the Phippses and to their exclusive advantage; that the names of the corporations were used as a shield to protect from persons with whom the Phippses dealt through the names of the corporations the information of the personal liability of the Phippses; that the nominal stockholders, officers and directors of the corporations are as such mere employees of the Phippses, who pay them for their activities in the said corporations and who are used for superficially maintaining a legal government of the corporations and their legal corporate entities, but in reality to shield and cover the interests of the Phippses in the many transactions intended to be entered into for their exclusive financial benefit and to guard them from personal liability to persons who in the course of such transactions became ostensibly creditors of one or more of such corporations; that The Third Avenue Company was thus a mere device in the hands of the Phippses for the purpose of giving them absolute control of the property ostensibly purchased by that corporation while protecting them from personal liability for any indebtedness included in the name of the corporate entity; that Mrs. Keely became a cred-

itor of The Third Avenue Company in one or more transactions with that corporation under the conditions set forth above" (111 Florida, pp. 48, 49).

The Trial Court had sustained the demurrer to the original bill. As to this ruling the Supreme Court of Florida said:

"The allegations of the original bill state a ground for equity relief upon the doctrine announced by this Court in the case of *Biscayne Realty and Insurance Co. v. Ostend Realty Company, et al.*, decided at this term and filed May 24, 1933.

* * * The bill stated such a case as would require a court of equity to look beyond the mere form of the corporate entity to the persons who were the sole beneficiaries of its activities, directed and managed its transactions, used the corporate name at pleasure, incurred financial obligations in its name, conveyed to themselves corporate lands, and other property as desired, received the profits, if any, paid out money as the transactions required, and in fact set up and treated the corporate entity as their principal. In such circumstances the interests of the corporation and its owners became so blended, so indistinguishable, as to be identical.

The instant case is distinguished from the *Biscayne Realty Insurance-Ostend Realty Company* case in no essential element. According to the allegations of the original bill the Phippses merely concealed themselves beneath one more layer of names. Instead of using their own names as stockholders and officers they merely employed others in their service to use theirs, but whom they directed and manipulated as pawns in their complicated and deceptive game of trade. Whether the allegations of the bill can be proved by the complainant is another matter, but the allegations of the bill set up such a case" (111 Florida, pp. 50, 51).

In the present case neither Scott, Alley, Hawkins nor Riley held any stock in the Seminole Boat Company nor were they in any way interested in that company, except as employees of Phipps. The Seminole Boat Company never had any financial independence and at all times was dependent for its existence upon the respondent for payment of its bills. It had no capital funds nor money of its own. John S. Phipps originally contributed $50 and Henry C. Phipps $50, not even enough to pay the expenses of organization. This was the only cash which the corporation ever had as its own. All other moneys were advanced either by Boulevard Mortgage Company or by the Palm Beach Company for the account of the Phippses and were repaid to the advancing companies by the Phippses.* Scott, Alley, Hawkins and Riley re-

*The following is an extract from Respondent's Exhibit 41 offered R. 1659, see reprint accompanying record which is respondent's own summary of the financial operation of Seminole Boat Company.

ANALYSIS OF OPERATION OF SEMINOLE BOAT COMPANY

PERIOD OCTOBER 11, 1928 THROUGH DECEMBER 31, 1935

On November 11, 1928 the records of account for Seminole Boat Company were set up with Journal Entry #1 recording the subscription payment and issuance of 10 shares of its capital stock as follows:

| | |
|---|---|
| S. L. Mackey | 4 shares |
| L. C. Chester | 3 shares |
| H. Kennedy | 3 shares |

On November 20, 1928, an account was opened with the First National Bank, Miami, Florida depositing $100.00, being the proceeds from the sale of the above listed stock.

The Boulevard Mortgage Company made cash advances to Seminole Boat Company, also paid sundry expense items for its account. Both the cash advances and disbursements for sundry expenses were set up on Seminole Boat Company records as Accounts Payable to Boulevard Mortgage Company. From time to time the Messrs. J. S. and H. C. Phipps would reimburse Boulevard Mortgage Company for

[Footnote continued on following page]

garded themselves as representatives of the Phipps family and were dependent upon the Phipps family for their employment and dared not incur any major expense for repairs of the "Seminole" without obtaining approval of the Phipps family. The Seminole Boat Company was without any credit of its own and the credit which was extended was extended to the Phippses. The Phippses retained the yacht "Seminole" to use it at their pleasure, and did so use it, without corporate action recognizing their rights.

In the spring of 1935, Hawkins, Secretary-Treasurer of the Company, on the instructions of respondent Phipps, bought a small vessel called a "Prig" boat for $950. On further instructions from respondent Phipps, the purchase price was charged to Seminole Boat Company. After the fire the "Prig" boat was transferred to the respondent Phipps by bookkeeping entries. A corporation with less

[Footnote continued from preceding page]

such items—one-half each. When such reimbursements were made the Seminole Boat Company would, by journal entry, transfer its liability to Boulevard Mortgage Company to the Messrs. J. S. and H. C. Phipps.

The cash advances by Boulevard Mortgage Company and other cash receipts were deposited in Seminole Boat Company's bank account with First National Bank, Miami. From this account were paid the principal operating expenses to June 2, 1934. On this date the bank account was closed and Boulevard Mortgage Company paid all operating expenses to December 31, 1933. Palm Beach Company then paid all operating expenses from this date on. The Messrs. J. S. and H. C. Phipps reimbursed Boulevard Mortgage Company and Palm Beach Company for such expenses to December 31, 1934. Their reimbursements were handled as stated in above paragraph. Mrs. Guest acquired the one-half interest of Mr. H. C. Phipps on March 23, 1935, Mrs. Guest assuming his one-half of the expenses for period January 1, 1935 through March 23, 1935. Mrs. Guest and Mr. J. S. Phipps reimbursed Palm Beach Company for expenses to March 23, 1935—one-half each.

independence and more completely the *alter ego* of the respondent Phipps, could hardly be imagined.*

The subsequent Florida cases follow the same doctrine:

*Hirsch* v. *Lincoln Securities Co.*, 118 Florida 164, 168 So. 12;

*Mayer* v. *Eastwood-Smith Co.*, 122 Florida 34, 164 So. 684;

*Fickling Properties, Inc.* v. *Smith*, 123 Florida 556, 167 So. 42;

*Bellaire Securities Corp.* v. *Brown*, 124 Florida 47, 168 So. 625;

*Wofford* v. *Wofford*, 129 Florida 445, 176 So. 499;

*Miakka Estates* v. *B. L. E. Corporation*, 132 Florida 307, 181 So. 423.

In these last two cases, the Supreme Court of Florida quotes with approval the following language from its decision in *Mayer* v. *Eastwood-Smith Co.*, 122 Florida 34, at p. 43, where the Court said:

> "The overwhelming weight of authority is to the effect that courts will look through the screen of corporate identity to the individuals who compose it in cases in which the corporation was [1] a mere device or sham to accomplish some ulterior purpose, or [2] is a mere instrumentality or agent of another corporation or individual owning all or most of its stock, or [3] where the purpose is to evade some statute or to accomplish some fraud or illegal purpose" (the numbers in brackets are supplied by us).

The decisions of the courts below ignored category [2] as a ground for piercing the corporate veil. Merely because the facts here did not establish a case under category [1] (or, as was said below, because there was no evidence of

* In Appendix B, attached to this brief, p. 57, we have summarized respondent's evidence as to the Phipps' domination of the corporation.

fraud "or other improper conduct or purpose in the creation or continued existence of the corporation", or "that the corporation was an artifice and a sham designed to execute illegitimate purposes") the courts below held that the respondent Phipps was not liable. Because the facts do not justify a holding under category [1] that the corporate veil was pierced, is immaterial, since they do establish that the veil was pierced under category [2].

The law applied by the Admiralty courts is the same. In the leading case in Admiralty, which was also a case of tort, the *Willem van Driel, Sr.*, 252 F. 35, cert. denied 248 U. S. 566, the Court permitted the corporate veil to be pierced for identically the same reason as that given by the Supreme Court of Florida in category [2] in *Meyer v. Eastwood-Smith Co.*, 122 Florida 34. In the *Willem van Driel, Sr.*, the Circuit Court of Appeals for the Fourth Circuit said that liability:

> "depends upon the question of fact whether the elevator company although in the name and organization a distinct corporation, was in substance a mere corporate agent or instrumentality of the Pennsylvania Railroad Company. *So. Pac. Terminal Co. v. Int. Comm. Com'n.*, 219 U. S. 525, 31 Sup. Ct. 279, 55 L. Ed. 310; *Joseph R. Foard Co. v. State of Maryland*, 219 Fed. 827, 135 C. C. A. 497; *Lehigh Valley R. Co. v. Delachesa*, 145 F. 617, 76 C. C. A. 307."

See also:

*Luckenbach S. S. Co. v. W. R. Grace & Co. Inc.* (C. C. A. 4), 267 Fed. 676;
*The Centaurus* (C. C. A. 4), 291 Fed. 751;
*The J. B. Austin Jr.* (E. D. N. Y.), 1 F. (2d) 451.

Judge Wallace in the Second Circuit said in *Lehigh Valley R. Co. v. DuPont* (C. C. A. 2), 128 Fed. 840, that,

"the potential and ultimate control" was the test. In none of these cases was fraud or illegitimate purpose an essential element in the case. The stockholder's liability rested upon the fact that the corporation lacked essential elements of corporate independence, and was subject to the domination and control of stockholder.

It is true that fraud may also be a ground for "piercing the corporate veil" and holding shareholders liable for the debts of the corporation, but since fraud can only be in an element in contract cases, category [1] is of no importance here. When a party voluntarily enters into a contract with a corporation, he knowingly contracts with the corporate entity, which has a limited liability. He cannot complain of that limited liability unless he can show that he has been misled or tricked or fraudulently induced to enter into a contractual relation with it. See:

*Roos* v. *Texas Co.* (C. C. A. 6), 43 F. (2d) 1;
*New York Trust Co.* v. *Carpenter* (C. C. A. 2), 250 F. 668, 673, 678;
*Weisser* v. *Marsam Shoe Corp.* (C. C. A. 2), 127 F. (2d) 344, 347, note 6.

Decisions in such cases have no application to tort liability. In tort cases there is nothing in the legal relations involved which admits of fraud as an element of liability.

Similarly there are cases where an improper purpose in the formation of a corporation may be sufficient for disregarding the corporate entity. The so-called bank stock cases may be cited as examples:

*Coker* v. *Soper* (C. C. A. 5), 53 F. (2d) 190, certiorari denied 285 U. S. 540;
*Harris Inv. Co. et al.* v. *Hood* (Fla.), 167 So. 25.

In tort cases the test is, was the corporation in fact an entity? Was it sufficiently independent of its shareholders and sufficiently free of their dominance and control to be regarded as more than a mere agent of the shareholders? We respectfully submit that the District Court was clearly wrong in holding that the Seminole Boat Company was not respondent Phipps under another name merely because no fraud was involved.

The test applied by the Circuit Court of Appeals of "artifice and sham designed to execute illegitimate purposes" is equally inapplicable.

That the corporate form does not effectively protect shareholders from tort liability when the corporation has no real independence, and the corporation is a mere name, is well established:

*Davis* v. *Alexander*, 269 U. S. 114;

*Callas* v. *Independent Taxi Owners Assn.* (C. C. A.), D. C., 66 F. (2d) 492; certiorari denied 290 U. S. 669;

*Mangan* v. *Terminal Transportation System, Inc.*, 284 N. Y. S. 183, 157 Misc. 627; aff'd 286 N. Y. S. 666, 247 App. Div. 853; appeal denied 272 N. Y. 676;

*Anglaize Box Board Co.* v. *Hinton*, 100 Ohio St. 505, 126 N. E. 881;

*Joseph R. Foard Co.* v. *State* (C. C. A. 4), 219 Fed. 827;

*Oriental Investing Co.* v. *Barkley*, 64 S. W. 80, 25 Tex. Civ. App. 543;

*Erickson* v. *Minnesota & Ontario Power Co.*, 134 Minn. 209, 158 N. W. 979;

*Specht* v. *Missouri Pacific R. R. Co.*, 154 Minn. 314, 191 N. W. 905;

*Dixie Coal M. & M. Co.* v. *Williams*, 221 Ala. 331;

*Ross* v. *Pennsylvania Railway Co.* (N. J.), 148 Atl. 741.

See also:

*Weisser* v. *Mursam Shoe Corp.* (C. C. A. 2), 127 F. (2d) 344 (Opinion with notes by Frank, *C. J.*; April 27, 1942).

No case could illustrate better than the instant case the injustice, and the harmful results, which will follow from the establishment of the rule laid down by the Courts below. Here the owner has thus far successfully avoided any responsibility for negligent operation of the yacht "Seminole" merely by creation of a corporation which was an empty shell. When "with the passage of time" gas tanks, always a serious hazard*, through lack of inspection and proper maintenance become defective and leaky and cause an explosion and fire which destroys a large number of vessels owned by innocent persons, such an owner should not under the circumstances of this case be permitted to hide behind the corporate veil. We submit, that to grant the immunity of corporate insulation in such a case, establishes a dangerous precedent and encourages the owners of yacht, or other vessel property, to employ this devious method of avoiding personal liability.

It cannot be said that the question of the control and domination of Seminole Boat Company by respondent Phipps is a question of fact decided by the lower Courts adversely to petitioners. Neither of the Courts below made any findings as to control and domination of the corporation by the respondent Phipps because in their view this was not important, in the absence of any showing of fraud or improper purpose in the creation or continued existence of the corporation.*

The facts admitted by respondent Phipps clearly establish that the Seminole Boat Company was no more than respondent Phipps under another name.

* See *Gunnarson* v. *Robert Jacob* (C. C. A. 2), 94 F. (2d) 170, 172 (Learned Hand, *C. J.*).

## II.

**Both courts below concurrently found that the losses sued for were caused by the negligence of Seminole Boat Company and that negligence consisted in permitting gasoline tanks to become defective and leaky "through the passage of time". Such a condition could not have existed if there had been proper inspection. Since, as we have shown, this negligence of the Seminole Boat Company was in fact the negligence of respondent Phipps, respondent Phipps is not entitled to limit liability. If the tanks had been examined the defective condition of the tanks would no doubt have been discovered. Knowledge of what could have been discovered, if a proper inspection had been made, is imputed to Phipps. The decision of the District Court that the character of the negligence, *i. e.*, "the failure to do or perform a duty, or non-feasance", did not constitute "privity and knowledge" and did not preclude Phipps "from asserting * * * limitation of liability under the statute", U. S. C. Title 46, §183, is clearly erroneous and is in conflict with the decisions of other circuits.**

The negligence of the Seminole Boat Company, which both courts below found was the cause of the losses sustained by petitioners, was in fact, as we have just shown, that of the respondent Phipps. That negligence consisted in permitting tanks to become defective and leaky "through the passage of time" (R. 3587; 39 F. Supp. at p. 144). In short, the petitioners' losses were due to the general decay of the yacht "Seminole"—decay which progressed with time. Nevertheless, the District Court held that if an owner's negligence consists of "the failure to do or perform a duty, non-feasance" (R. 3587; 39 F. Supp. 144), he may still limit his liability. Since the "Seminole"

after the explosion was a worthless wreck, this decision really exonerates Phipps from all liability.

Contrast the language of the District Court with that of the Courts in the following cases:

In *Chesapeake Lighterage & Towing Co., Inc.* v. *Baltimore Copper, etc. Co.* (C. C. A. 4), 40 F. (2d) 394, 395, the Circuit Court of Appeals for the Fourth Circuit said:

> "For authorities on the law that controls the question of privity or knowledge of the owner, reference to *The Virginian* (D. C.) 264 F. 986,* *Sorenson et al.* v. *Boston Insurance Co. of Boston, Mass.*, 20 F. (2d) 640, and *Bank Line* v. *Porter, (The Polaric)* 25 F. (2d) 843 will show the rule as laid down by this court. Under these decisions the judge below rightly held that the superintendent of the appellant company could, by proper inspection, have discovered the unseaworthiness of the barge, and that the appellant was therefore chargeable with knowledge of such unseaworthiness."

In *Sabine Towing Co.* v. *Brennan* (C. C. A. 5), 72 F. (2d) 490, at page 493, where an old tug, which was covered by certificates stating that she had been inspected and found fit, sank in weather, which she should have withstood, and caused the loss of a number of lives, the Court held that the owners were not entitled to limitation of liability. The Court went on to say that such difficulty as there was in the case was whether the petitioner was entitled to exoneration altogether, rather than whether he was entitled to limitation, because if negligence existed, its very nature was such that the petitioner could not limit against it. The Court said:

> "We think it plain, in fact, the record leaves no room for question, that whatever may be said in

* Cited with approval in *Spencer Kellogg Co.* v. *Hicks*, 285 U. S. 502 at p. 511.

favor of exoneration altogether, because of failure to prove negligence, this is not a case for limitation of liability. Whatever was done with the tug of about it was the act of the owner through its managing officers, and if there was negligence, the owner was privy to it. All of those who testified for appellant make this clear. While they testified positively that Guy was the port engineer and in charge of repairs, they testified too that he made no serious repairs without consulting the officers, and that everything that was done by him in actually equipping this vessel was done under their supervision, and with their approval. Under these circumstances, if there was negligence, the officers were privy to it, and appellant, present in the presence of its managing officers, was privy to it too. *Ft. Worth Elevators Co. v. Russell* (Tex. Sup.) 70 S. W. (2d) 397; *In re N. Y. Dock Co.* (C. C. A.) 61 F. (2d) 777; *Henson v. F. & C. Trust Co.* (C. C. A.) 68 F. (2d) 444; *The Malcolm Baxter, Jr.*, 277 U. S. 323; 48 S. Ct. 516, 72 L. Ed. 901; *The Mamie* (D. C.) 43 F. (2d) 562; *The Vestris* (D. C.) 60 F. (2d) 273; *Kellogg & Sons v. Hicks*, 285 U. S. 511, 52 S. Ct. 450, 76 L. Ed. 905, (72 F. (2d) at p. 493).

See also *The 84 H.* (C. C. A. 2), 296 Fed. 427, cert. den. 264 U. S. 596.

Here it was an expensive matter to get at the tanks on account of the coal bunkers. Mr. Hawkins testified that he would not make any repairs to the "Seminole" beyond the sum of $500 without consulting the respondent Phipps, and Riley said that he could not order repairs in excess of $200 without consulting Phipps.* In these circumstances the tanks could not be thoroughly inspected without Phipps' consent.

* See Appendix B, p. 65, *infra*.

See also *In re Jacobsen*, 32 F. (2d) 179 at p. 180, and *The Friendship II (Just v. Chambers)* (C. C. A. 5),* 113 F. (2d) 105 at p. 107, where the Court said:

> "Responsibility for the injury having been established, it remains to be determined whether the appellant is entitled to a limitation of liability. Since a proper inspection of the vessel would have shown the defective condition of the pipes, and Yeiser was himself present and in charge, the injuries were not occasioned without the knowledge or privity of the shipowner. *Because he failed to make such an inspection he may not have limitation. The Republic*, (2 Circ.) 61 Fed. 109; *Christopher v. Gracha*, 40 F. (2d) 8."

See also the decisions of the Circuit Court of Appeals for the Second Circuit in *The Republic* (C. C. A. 2), 61 F. 109; *In re Jeremiah Smith & Son* (C. C. A. 2), 193 F. 395, and *In re P. Sanford Ross* (C. C. A. 2), 204 F. 248.

In *The Malcolm Baxter, Jr.* (C. C. A. 2), 20 F. (2d) 304, 305, the same Court denied limitation because structural defects existed, which, although not found by surveyors, could have been discovered by due diligence. This latter case was affirmed by this Court in *The Malcolm Baxter, Jr.*, 277 U. S. 323, at p. 332. There this Court said:

> "Respondents had purchased the vessel about one month before she sailed. At that time she was unseaworthy, due to a 'hog' or camber in her keel, a struc-

* The decision of the Circuit Court of Appeals, although it affirmed that of the District Court on the issues of negligence and limitation, reversed the decree of the District Court awarding damages to injured persons on the ground that because the tort-feasor had died, the cause of action abated with his death. Certiorari was granted by this Court, and in *Just v. Chambers*, 312 U. S. 383, the judgment awarding full damages, without limitation, of the District Court was restored.

tural weakness dangerous to the ship in heavy weather, which later caused the leak and made necessary the repairs at Havana. Following the purchase and before sailing from New Orleans a survey was made by the owner, which appears not to have disclosed her condition, but both courts below agree that the fact of her unseaworthiness could have been discovered by due diligence" (277 U. S. 332).

And, at page 331 of 277 U. S., this Court said:

> "Both courts below agreed that the 'Baxter' was unseaworthy on sailing and that respondent failed to exercise due diligence to ascertain her condition before sailing. This was sufficient ground for denying the petition for exoneration and limitation of liability under the Harter Act, Act of February 13, 1893, c. 105, 27 Stat. 445, and acts permitting limitation of liability to the vessel and pending freight, R. S. 4282-4289."

In the case of *The Isoud* (C. C. A. 2), 294 F. 930, Judge Ward, in his concurring opinion denying limitation of liability, said:

> "There is no proof of any regular system of inspection by any one, or *that its managing officers relied upon a competent person, to whom the duty of regular inspection was committed.*"

In *Porter-Carpenter Coal Co. v. New York, O. & W. Ry. Co., et al.* (S. D. N. Y.), 50 F. (2d) 270, the Court said:

> "It is my opinion that there should be no limitation of liability in this case. Limitation is permissible only where the owner can show lack of knowledge or privity of the unseaworthy condition. The burden of proving such lack of knowledge or privity is on the owner. *In re P. Sanford Ross, Inc.* (C. C. A.), 204

F. 248; *In re Reichert Towing Line* (C. C. A.), 251 F. 214. Where the unseaworthiness is due to a generally decayed condition of the vessel which renders it unable to withstand the ordinary wear and tear of service, as was the case with this old barge, *the owner's lack of knowledge can only mean that the owner did not inspect the vessel or provide a regular system of inspection. The Republic* (C. C. A.), 61 F. 109; *In re P. Sanford Ross, Inc., supra.*"

Similarly, in the case of *The Miami* (E. D. N. Y.), 43 F. (2d) 562, the Court said:

> "These defects, of a most serious nature, had existed for a long time, and were structural. *In re P. Sanford Ross, Inc.* (C. C. A.), 204 F. 248-252. The company should have informed itself of this very apparent condition. *The Republic* (C. C. A.), 61 F. 109-113.
>
> There is no proof that there was any serious system of inspection or reliance upon any really competent person for that purpose.
>
> Under such circumstances not only has there been a failure of proof on the part of the petitioner, but the facts all indicate a situation that may well raise a presumption that the corporation must be presumed to have had knowledge of her condition. See *In re P. Sanford Ross, Inc.*, 204 F. 248 (C. C. A. 2)."

See also the very recent case in the Circuit Court of Appeals for the Second Circuit, *New York & Cuba Mail S. S. Co. v. Continental Ins. Co.* (C. C. A. 2), 117 F. (2d) 404, at p. 409.

Judge Hough in *The Argent*, 1940 A. M. C. 508, at p. 509, summed up the matter thus:

> "It would, however, be a very easy matter for an owner to shelter himself behind an actual ignorance if lack of personal knowledge always constituted a

good defence to the extent of the protection accorded by statute. If lack of actual knowledge were enough, imbecility, real or assumed, on the part of owners, would be at a premium. Such assumption of ignorance would be peculiarly easy on the part of corporate owners. Corporate owners have of late years greatly multiplied, and it is accordingly found that the doctrine of imputed knowledge and imputed privity has grown to meet the demands of business.

. . . . . .

As long ago as *Republic*, 61 Fed. 109, knowledge of what owners could have seen if they had looked was imputed to them. The same doctrine is assumed in *Towson*, 142 Fed. 1034; it is assumed in *Re Smith*, 193 Fed. 395, and fully applied under circumstances which in substance are very like this in *Re Santord Ross*, 204 Fed. 248.

*Parsons* v. *Empire Transportation Co.*, 111 Fed. 202, certiorari denied, 183 U. S. 699, is authority for considering Conway as the managing agent or *alter ego* of the corporation. Personally I prefer the doctrine of imputed knowledge, but the result is the same."

In short, contrary to what the District Court held, the law in the United States is that where a vessel through the passage of time has become defective, the owner may not limit liability if the defects could have been seen if looked for.

The failure of an owner to inspect, or to provide an adequate system of inspection by competent persons, is sufficient to deprive an owner of the benefits of the statute. See Benedict on Admiralty, Fifth Edition, Sec. 498, as follows:

"*Neglect to inspect the vessel or properly to provide a system of inspection* creates ordinarily such privity with a disaster arising from a defective con-

> dition of the vessel as to preclude limitation and, where the owner has delegated power to a shipmaster or other agent and has relied upon him to see to it that the vessel is properly equipped or otherwise fitted for the contemplated service, *the burden of proving the competency of such representative* for the work entrusted to him rests upon the owner and, unless such competency is affirmatively shown, the owner cannot limit his liability.*

In cases such as *The Republic*, and *The Malcolm Baxter, Jr., supra*, where the defects were of long standing, *i. e.*, decay in the "Republic", and a hog or camber in the "Malcolm Baxter, Jr." limitation was denied because a proper inspection was not had. Both in *The Malcolm Baxter, Jr.* and in the *Sabine Towing Co.* cases, surveyor's certificates had been issued, yet that did not save the shipowner. Neither does the certificate of Surveyor Bernard** save the respondent in this case. Bernard visited the engine room of the yacht for only about fifteen minutes (R. 2246, 2225). He was afforded no facilities for inspection. There being no captain or engineer on

* See also Benedict on Admiralty, Sixth Edition, Vol. III, pp. 385-7.

** Bernard was the surveyor to whom the Circuit Court of Appeals referred in the passage reading:

> "It is undisputed that the vessel had been examined and pronounced fit by an experienced ship surveyor in February, 1935; that she developed no flaws during the cruise or prior to reaching Pilkington's; that the crew left her gasoline valves closed, her electric switches open, her gas tanks registering empty, and her bilges clean and free of gasoline or gasoline vapor; and that she was repeatedly examined by competent men between April 15 and June 24, 1935, who discovered nothing wrong with her." (R. 3647, 128 F. (2d) 703).

We do not know what the Court means by saying that these statements were not disputed, since we have contested them from the outset. We now repeat that there is not a scintilla of evidence which supports the Court's statement that the yacht "was repeat-

(Footnote continued on following page.)

board, he could not operate any of the machinery or controls in the absence of an owner's representative (R. 2225, 2228-9). He was not employed to make a thorough examination or "condition survey" (R. 2224, 2231). He did not and could not examine the tanks which leaked, because of their inaccessibility (R. 2215, 2231, 2248, 9). He received for his services the paltry sum of $17.50 (R. 1430). He conceded that his examination was superficial and that he did not intend it for a thorough examination, or represent it as such (R. 2224). Moreover, he testified that the construction of the yacht was such that only a small portion of the surface of the four cylindrical tanks, which the Court found leaked, could be seen or inspected (R. 2248-9). These tanks were contained in the old coal bunker, which they completely filled, and the only way that one could see the tanks would be to remove one of the steel walls of the bulkhead forming the coal bunker. Bernard testified that he would have charged about $25 for a proper survey, and that to place the yacht in proper condition after such survey, would have cost the owner $2,500 or more (R. 2238).

The inaccessibility of the tanks does not excuse failure on the part of the respondent to inspect them, nor his failure to take such measures as were required to pre-

[Footnote continued from preceding page.]

edly examined by competent men between April 15th and 24, 1935, who found nothing wrong with her". In fact, the opposite is the case, for it is a fact that no one examined the "Seminole" from the time she was laid up on April 16, 1935 to the day of the fire. Later in the opinion the Circuit Court of Appeals concurred in the findings of the District Court and held that petitioners' losses were due to negligence of the Seminole Boat Company. This finding disposes of any inference from the remarks quoted to the effect that the shipowner had done all that it should have done in connection with the inspection of the "Seminole", because if the shipowner had done so, the Court's subsequent finding of negligence would be meaningless.

vent their becoming defective through lapse of time since their installation thirteen years before the fire, *i. e.*, 1922. Neither is it any excuse to say that this was the best places for them. A somewhat similar situation was discussed in *Gunnarson* v. *Robert Jacob* (C. C. A. 2), 94 F. (2d) 170, at page 172, where the Court, speaking through Judge Learned Hand, said:

> "But to say that such a tank was safest where it was put, is not to say that it was safe at all, and we do not think that it was, without more care on the owner's part. *It is of no moment that it was harmless so long as it did not leak, and that it would not leak if it was properly handled. In such cases liability depends upon an equation in which the gravity of the harm, if it comes, multiplied into the chance of its occurrence, must be weighed against the expense, inconvenience and loss of providing against it. The harm may be so great as to impose an absolute liability, regardless of any negligence;* in such cases the very activity, though lawful, entails responsibility, and reparation becomes a cost of the enterprise, as under workmen's compensation. *Exner* v. *Sherman Power Construction Co.*, 2 Cir., 54 F. (2d) 510, 80 A. L. R. 686."

It is common knowledge that gasoline used for driving an explosion engine, is dangerous, and, as Judge Hand says in the passage just quoted, although it may have been safer to put these tanks in an old coal bunker, where they would be protected from blows or other contacts with objects which would be likely to damage them, such protection would be of no moment if the tanks did actually leak.

Before concluding the argument under this heading, because the language is so apt, we call the decision in

*Asiatic Petroleum Company, Ltd.* v. *Leonard's Carrying Co., etc.** (1914), 1 K. B. 419, to the Court's attention.—

> Buckley, *L. J.*: "If the owner be guilty of an act of omission to do something which he ought to have done, he is no less guilty of "actual fault" than if the act had been one of commission. To avail himself of the statutory defense, he must shew that he himself is not blameworthy for having either done or omitted to do something or been privy to something. It is not necessary to show knowledge. If he has means of knowledge which he ought to have used and does not avail himself of them, his omission so to do may be a fault, and, if so, it is an actual fault and he cannot claim the protection of the section" ([1914] 1 K. B. at p. 432).

The reasons given in the instant case by the District Court to sustain its holding of absence of privity are the same as those given by Buckley, *L. J.*, for holding that there was privity. And in the same case, Hamilton, *L. J.*, took a similar position to that of Buckley, *L. J.*, when he said:

> "I recall with proper diligence the owners might have prevented all this and must have known the special perils attending the transport of benzine in bulk, for it was their trade. When those owners ask this Court to find that the fire, which naturally ensued in the circumstances 'happened without their actual fault or privity', I refuse." (1914) 1 K. B. 441.

It is true that the yacht "Seminole" was not in the trade of carrying benzine, but it did burn large quantities

* Vaughan Williams, *L. J.*, dissented from the judgment of Buckley, *L. J.*, and Hamilton, *L. J.* The case, under the style of *Leonard's Carrying Company, Limited* v. *Asiatic Petroleum Company, Limited* (1915), A. C. 705, went to the House of Lords, which unanimously affirmed the decision below. In the course of his speech, Lord Dunedin specifically approved the ground upon which Hamilton, *L. J.*, placed his judgment.

of gasoline which it did carry in "defective" tanks. Respondent Phipps must have known the special perils attending gasoline. Those perils are matters of common knowledge. Obviously, with proper diligence these tanks would not have become defective. They could have been kept sound and tight. The fact that they were not, and that they leaked, and gasoline later exploded, were circumstances which naturally ensued. We submit that Hamilton, *L. J.*, was right when he refused to say that such circumstances happened without the privity and knowledge of an owner. The circumstance that the owner was ignorant of what he should have known, and neglected to provide any means which would enable even a visual examination of the tanks, much less a thorough test, is enough under the authorities cited above to deprive him of the benefits of the limitation statute.

For these reasons alone limitation should have been denied.

## III.

**The decision of the Circuit Court of Appeals that the respondent Phipps, if liable, is entitled to the protection of the limitation of liability statute, on the ground that privity or knowledge of the defective condition of the yacht "Seminole" could not "be imputed to him since he had exercised due care and diligence in selecting competent men to man the vessel, and had imposed on them full duties as to inspection and maintenance of her" is erroneous and is in conflict with the decisions in the Second, Sixth and Ninth Circuits. When the owner of the "Seminole" delegated full "duties as to inspection and maintenance" to these men, they became the owner's *alter ego*, and their knowledge and privity became the knowledge and privity of the owner.**

In its opinion the Circuit Court of Appeals held that the respondent Phipps, if liable personally, was entitled to limitation of liability, because

> "the evidence affirmatively establishes that no actual privity to or knowledge of the defective condition obtaining on the 'Seminole' was attributable to Phipps personally, and that none could be imputed to him since he had exercised due care and diligence in selecting competent men to man the vessel, and *had imposed upon them full duties as to inspection and maintenance of her*" (R. 3649).

We do not concede that the men selected to man the vessel were competent. But even if they were competent, when the owner "imposed upon them full duties as to inspection and maintenance" they became the *alter ego* of the owner and their privity became that of Phipps.

The decisions of the Circuit Courts of Appeal in the Second, Sixth and Ninth Circuits so hold.

The Circuit Court of Appeals for the Second Circuit in the case of *In re New York Dock Co.* (C. C. A. 2), 61 F. (2d) 777, held that one, Converse, who, under R. S. 4286 was, in legal effect, the owner of a pile driver, could not limit liability because of the negligence of his superintendent, who was in complete charge of the inspection and rigging of the barge.

The Court said at page 779:

> "*So the scope of the authority delegated to Mc[illegible]by Converse was so broad that his privity or knowledge as to the unseaworthiness of the pile driver was in law that of Converse.* *Spencer Kellogg & Sons v. Hicks*, 285 U. S. 502, 52 S. Ct. 430, 76 L. Ed. 903; *In re P. Sanford Ross* (C. C. A.), 294 F. 248; *Chesapeake Lighterage & Towing Co., Inc. v. Baltimore Copper Smelting & Rolling Co.* (C. C. A.), 40 F. (2d) 394; *Boston Towboat Co. v. Darrow-Mann Co.* (C. C. A.), 276 F. 778."

The decision below is also in conflict with that of the Circuit Court of Appeals for the Ninth Circuit in *The Silverpalm* (C. C. A. 9), 94 F. (2d) 776, where that Court dealing with a similar situation, said at page 780:

> "In proceedings for limitation the owner may not escape liability by giving the managerial functions to an employed person acting as its agent, *whether the person be corporate or otherwise.* *So far as concerns privity and knowledge, such an agent is its alter ego.* *Craig v. Continental Ins. Co.*, 141 U. S. 638, 648, 12 S. Ct. 97, 35 L. Ed. 886; *Eastern S. S. Corporation v. Great Lakes Dredge Co.* (C. C. A. 1), 256 F. 497, 502; *Sperry Flour Co. v. Coastwise S. S. Co.* (C. C. A. 9), 84 F. (2d) 785, 786."

The decision below is also in conflict with that of the Circuit Court of Appeals for the Sixth Circuit in

IN THE

# Supreme Court of the United States

**OCTOBER TERM, 1942.**

**No. 246.**

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CHARLES CORYELL, *et al.*,

*Petitioners,*

—against—

JOHN S. PHIPPS and GEORGE J. PILKINGTON,

*Respondents.*

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## REPLY BRIEF ON BEHALF OF PETITIONERS.

As is not infrequently the case, counsel for the respondent seeking to avoid review by this court of the decisions below asserts in the Brief for Respondent that the questions presented by the petition are of fact only. It is significant that in their statement of the facts and of the findings of the District Court, respondent's counsel has considered it necessary to make two assertions, which are at variance with the record.

At page 7 of the Brief for Respondent Phipps, it is suggested that the cause of petitioners' losses was the negligence of one Abel. It is noteworthy that none of the references in the brief in support of this suggestion is from the finding of either of the courts below. Indeed, the District Court found the exact contrary,—that negligence of Abel was not the proximate cause of the loss (R. 3587).

Similarly, at page 6 of the Brief for Respondent Phipps it is asserted that the District Court "made no findings as to the cause of the fire * * *." This assertion is

based solely on the fact that the findings made by the District Court as to the cause of the fire do not appear in separately numbered paragraphs in the document filed by the District Court on June 5th, 1941 entitled: "FINDINGS OF FACT AND CONCLUSIONS OF LAW" (R. 3582), but do appear in the paragraphs following the subtitle "Discussion" and preceding the heading "Conclusions of Law". Regardless of formality of arrangement, we submit that the findings by the District Court in these paragraphs are, in fact, the findings of the District Court of the ultimate facts of the case and were so intended. The findings in the preceding numbered paragraphs are not findings of the ultimate facts but merely summaries of evidence. In fact, the words "I find" do not appear in the numbered paragraphs but do precede the subsequent findings on which we rely. They are not to be disregarded as findings because of "inartificial" arrangement. *Nashville Interurban Ry. v. Barnum*, 212 Fed. 634, 639.

In the recent case of *Commercial Molasses Corp.* v. *New York Tank Barge Corp.*, both this Court and the Circuit Court of Appeals treated a statement by the District Court in its Conclusion of Law No. 2 to the effect that on the evidence "the cause of the accident has been left in doubt" as, nevertheless, a finding of fact. *Commercial Molasses Corp.* v. *New York Tank Barge Corp.* (C. C. A. 2), 114 F. (2d) 248, 250; 314 U. S. 104, 114.

At R. 3587 the District Court said:

> "The presence of gasoline fumes in the engine room, *I find* was the proximate cause of the damage done to the vessels of libelants."*

Again, in the following paragraph, the District Court said:

> "But with the passage of time some part of the machinery or equipment did leak and the great possibility of damage attendant upon the use of gaso-

* Italics in quotations ours throughout this brief.

line, brings into play the principle that negligence may be based upon circumstantial evidence alone. The respondent argues that there must have been some third person agency intervening which brought about the means whereby gasoline escaped with attendant fumes. There is no evidence of this, and we get into the realm of conjecture. Just when the defective condition of the tanks made them leaky is in doubt. Expert testimony on this is an unsatisfactory character of evidence. *I am satisfied, and find,* that there were gasoline fumes present in the engine room, and that their ignition into combustion and fire caused the damage" (R. 3587-8).

We submit that these are findings by the District Court as to the cause of the fire; that the District Court did find that the presence of gasoline fumes in the engine room "was the proximate cause of the damage done to the vessels of libellants" (R. 3587), and that these fumes resulted because "with the passage of time some part of the machinery or equipment did leak" (R. 3587); that prior to the fire "the defective condition of the tanks made them leaky" (R. 3588) and that the presence of the gasoline fumes in the engineroom and "their ignition into combustion and fire caused the damage" (R. 3588).

We submit further that these findings cannot be disregarded as such for the reasons stated in the brief of the respondent Phipps.

Not only did the District Court make these findings with respect to the cause of the fire, but the District Court further found that the existence of these conditions was the result of negligence of Seminole Boat Company, Phipps' puppet corporation. At R. 3588, the District Court found "For this the Seminole Boat Company was liable". On the same page, a little farther on, because of its erroneous view of the law as to the liability of the respondent Phipps for the negligence of his creature corporation, the Court held that Phipps was not chargeable with that negligence "Firstly, because the negligence was that of the Seminole Boat Company and not of Phipps;".

It was similarly argued in the Circuit Court of Appeals that the findings of the District Court to which we have referred were not proper findings. The Circuit Court of Appeals not only did not accept this argument but itself adopted the findings of fact made by the District Court (R. 3647-8).

We have pointed out in our petition and brief that the District Court made its findings and reached its conclusion that the respondent Phipps was not liable for the negligence of the corporation on the sole ground that there was "no fraud or other improper conduct or purpose in the creation or continued existence of the corporation" (R. 3589) and because the organization of the corporation was "free from any fraud or ulterior motive in the inception of its chartering and creation" or other elements "incident to the presence of bad faith" (R. 3587; Petition, pp. 6 and 7), and that because of this erroneous view of the law neither of the courts below made any findings as to control and domination of the corporation by the respondent Phipps (Brief for Petitioners, pp. 27-8).

Nevertheless, it is asserted in the brief for the respondent Phipps that the real question presented is—"Did respondent in fact so dominate the corporate owner of the 'Seminole' that the corporate entity had been abandoned and should be disregarded?" (Respondent's Brief, p. 10) and it is asserted "This presents only a question of fact which both Courts below found favorably to respondent" (p. 10).

On the following page, it is asserted the Courts below concurrently found these facts against petitioners. In support of this assertion, it is stated that "Petitioners' contention as to domination was squarely presented below—see the excerpt from our main brief in the Circuit Court of Appeals printed *infra* as Appendix A" (Respondent's Brief, p. 17). Obviously the question as to what was found by the Courts below is not to be determined by consideration of the arguments or briefs presented but by examination of the decisions themselves.

The statement that the Courts below found against petitioners on the issue of domination cannot be justified. A careful scrutiny of the findings of both Courts will show that no finding was made by either Court on the question of the domination of the corporation or of corporate independence.

In the absence of any findings by either the District Court or the Circuit Court of Appeals on the questions of domination or corporate independence, we have summarized the facts in connection with the corporate ownership of the "Seminole" at pages 2 to 5 of the petition, supplementing the findings of the District Court only by statements of undisputed facts taken from respondent's own evidence and largely taken from respondent's own summary of those facts, Respondent's Exhibit 4D, printed as Appendix A to the Petition and Brief for Petitioners.

These supplementary statements are not materially disputed in the respondent's brief. They are discussed at pages 11 to 14 of respondent's brief, where they are merely characterized as "assertions" and "complaints" and an attempt is made to minimize their significance. Taken together, the conceded facts, which we have recited from the respondent's own evidence, clearly establish, we submit, complete lack of all essentials of corporate independence in Seminole Boat Company, and for the reasons, and under the authorities, cited in the petition and brief, establish the liability of the respondent Phipps for the negligence of the corporation.

In the respondent's brief, an attempt is made by brief and inadequate summary to minimize or distinguish the authorities cited in the petition and brief relative to the liability of the corporate parent, individual or corporate, for the negligence of a creature corporation. The decisions which we have cited speak for themselves and have been discussed in the brief and petition. We shall not burden the court with further discussion of these authorities.

We have shown in our petition and brief that although each of the Courts below expressed the opinion that the respondent Phipps, if liable, would be entitled to limitation of liability, each based this expression on a ground in conflict with the decisions in the other circuits. The grounds for the expression of opinion by the two courts were, however, different.

The Circuit Court of Appeals based its expression of this opinion on the proposition that

> "no actual privity to or knowledge of the defective condition obtaining on the 'Seminole' was attributable to Phipps personally, and that none could be imputed to him since he had exercised due care and diligence in selecting competent men to man the vessel, and *had imposed upon them full duties as to inspection and maintenance* of her" (R. 3649).

The Circuit Court of Appeals in this statement adopts the view that complete delegation of an individual owner's responsibilities and duties to a competent* person, or persons, assures limitation of liability irrespective of the negligence, knowledge or privity of those persons.

We have shown in the Brief for Petitioners (pp. 28-30) that this view is in direct conflict with the decisions in the Second, Sixth and Ninth Circuits, which hold that where an individual owner completely delegates his duties and responsibilities for the inspection and maintenance of his vessel to another, that other is the owner's *alter ego*, and the privity and knowledge of that other is the privity and knowledge of the owner.

*In re New York Dock Co.* (C. C. A. 2), 61 F. (2d) 777, 779;
*The Silverpalm* (C. C. A. 9), 94 F. (2d) 776, 780;
*In re Lakes Transit Corp. and James Playfair*, (C. C. A. 6), 81 F. (2d) 441, 444.

* There is in fact no evidence in the record to support a finding that the persons referred to, *i. e.*, the officers and directors of the corporation, were competent.

Counsel for respondent Phipps supports the view expressed by the Circuit Court of Appeals and asserts that there is in this respect a difference between the position of a corporate and an individual owner (Respondent's Brief, p. 19). The cases do not, in fact, justify this contention and the decision of the Circuit Court of Appeals for the Second Circuit in *In re New York Dock Co.* (C. C. A. 2), 61 F. (2d) 777, is directly to the contrary. Respondent's counsel naively asserts that in that case "the court overlooked" the fact that the owner was an individual, an assumption which can hardly be justified.

As pointed out by Hutcheson, *C. J.*, in the case of *In re Jacobson* (S. D. Tex.), 52 F. (2d) 178, 180, there is no logical justification for the contention of respondent's counsel. Judge Hutcheson said:

> "It is my opinion that those decisions are illogical which hold that, where an owner delegates the job of furnishing a seaworthy vessel to another, he may have limitation but that, where he tried to make it seaworthy himself, he may not have."

The late Judge Hough in characteristicly vigorous language dealt with a similar situation in the case of *In re Phoenix Sand & Gravel Co.* (S. D. N. Y.), reported 1940 A. M. C. 508, 509, when he said:

> "If lack of actual knowledge were enough, imbecility, real or assumed, on the part of the owners, would be at a premium."

Although this was a case of corporate ownership, it is clear that Judge Hough had in mind individual as well as corporate owners, for he followed this statement by saying:

> "Such assumption of ignorance would be particularly easy on the part of corporate owners."

Respondent's counsel asserts that the acceptance of a position contrary to his contention, "Would destroy the limitation statutes so far as individual owners are con-

cerned as fully as if Congress repealed them". There is no justification for this statement. There is justification for holding the individual owner to at least as high a degree of personal responsibility as a corporate owner.

It can hardly be contended that the agents to whom the respondent Phipps delegated his responsibilities as owner, *i. e.*, the officers and directors of his creature corporation, were free from negligence or privity and knowledge, in view of the fact that for a period of years prior to the disaster they had redelegated "control and management" as well as the duty of regular inspection to Riley, who was concededly inexperienced and incompetent to inspect (R. 1454-7, 1472, 1480, 1595-6, 1637, 1640-1).

The ground stated by the District Court for the expression of its opinion that the respondent Phipps, if liable, would be entitled to limitation of liability is set forth in the following quotation from the opinion:

> "The character of negligence shown by this record was such that Phipps, as an individual, would not be precluded from asserting as a limitation of liability under the statute" (R. 3588).

The "character of negligence" which the District Court had in mind is not disclosed in this paragraph of the opinion but is characterized on the preceding page as "the failure to do or perform a duty, or non-feasance" (R. 3587). While this statement was made in connection with the District Court's discussion of "corporate insulation", in the absence of any other or different characterization of the negligence in the subsequent passage, it can only be inferred that it was the same type of negligence to which the Court referred in connection with limitation of liability. Otherwise, the expression of the District Court is unexplained, and therefore meaningless.

We have shown in our petition and brief that the expression of opinion by the District Court that the character of negligence shown by the record as specified by the District Court, *i. e.*, the failure to do or perform a duty,

or non-feasance was not sufficient to preclude the respondent Phipps as an individual from limitation of liability under the statute, is in conflict with the decisions in the Second, Fourth and Ninth Circuits (Petition, pp. 15 to 17, 28; Petitioners' Brief, pp. 32-33). The decisions in those circuits hold that non-feasance consisting of the failure on the part of the owner in his duty to inspect the vessel, and to provide an adequate system of inspection by competent persons, results in the imputed knowledge and privity of the owner to the defective condition of his vessel, which requires the denial of a plea for limitation of liability. In the present case, it is the respondent's own evidence that the only system of inspection which had been provided for the "Seminole" for a period of years before the disaster consisted of the delegation by the officers and directors of the corporation, to whom respondent Phipps had entrusted the management of his vessel, of control and management and the duty of regular inspection to Riley, who was concededly inexperienced, and incompetent to inspect the vessel (R. 1454-7, 1472, 1480, 1595-6, 1637, 1640-1). The burden of proof was, of course, on the respondent Phipps to establish every element necessary to warrant a finding of the absence of privity and knowledge, including the fulfillment of his duty to provide both competent management and a regular and adequate system of inspection by competent persons (see summary of authorities, *The Silverpalm*, 94 F. (2d) 776, 777).

The suggestion that the innocent libellants, whose vessels have been destroyed, cannot complain of the lack of adequate inspections or of any system of inspection by competent persons because "an inspection was in progress at the time their loss occurred" (Respondent's Brief, p. 23) is specious indeed. Not only did their loss result from failure of inspection and failure to provide an adequate system of inspection by competent persons over a long period of time, but Abel, who is characterized as "an experienced boat captain", was not the captain of the "Seminole", and had had no previous connection with her.

He had been captain (by courtesy only) of much smaller vessels. There is no evidence other than the assertion of counsel that he was a competent or proper person to inspect the "Seminole". Even if the assertion in respondent's brief that "a system of inspection by the master has been held to be enough" (Respondent's Brief, p. 23) were accurate, which we question, Abel would not be within such decision since he was not master of the vessel.

The inspection of the "Seminole" in March, 1935, by a marine surveyor referred to in Respondent's Brief, page 23, was wholly inadequate, in particular, because he did not, and could not, under the conditions, examine the gasoline tanks which the District Court held became defective and leaky (R. 2215, 2248-9). He did not and could not under the conditions make any general examination of the vessel (R. 2231). It was not a thorough examination or a condition survey (R. 2224-5, R. 2228-9, R. 2236-8, R. 2246). He estimated from his examination at that time that it would have cost the owner about $2,500 to bring the "Seminole" to A-1 condition, which a condition survey would have required (R. 2238).

We submit, therefore, that the petition should be granted, and a writ of certiorari issued, and that this Court should review the decision of the Circuit Court of Appeals for the Fifth Circuit in this case so that the decisions and the law in admiralty cases in the various circuits may be reconciled on the important questions involved in this case as to the liability of an individual, who creates a corporation without corporate independence for the operation of his vessel, and who seeks limitation of liability by attempting to divest himself of his responsibilities as a vessel owner by delegation of those responsibilities to subservient employees through the use of the corporate device.

Respectfully submitted,

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